



STATE OF WASHINGTON

## ECONOMIC AND REVENUE FORECAST COUNCIL

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February 3, 2004

**TO:** Governor's Council of Economic Advisors

**FROM:** Chang Mook Sohn, Executive Director  
Office of the Forecast Council

**SUBJECT: PRELIMINARY JANUARY ECONOMIC FORECAST**

This preliminary forecast was based on Global Insight's January Control forecast for the U.S. economy. You should have received a summary of the Global Insight forecast by email. If not, please contact our office. The forecast was produced prior to the advance GDP estimate for the fourth quarter of 2003. According to the advance estimate, real GDP grew at a 4.0 percent rate in the fourth quarter of 2003 compared to 4.7 percent in the January forecast. Employment grew in the fourth quarter for the first time in a year though only at a 0.6 percent rate. The forecast correctly assumed the Fed would leave its target rate unchanged at 1.00 percent in January. The forecast assumes a 50 basis point increase in the federal funds rate in the third quarter which is earlier and sharper than assumed in November. The new national forecast for GDP, employment, and income is slightly stronger than the forecast adopted in November but inflation is lower.

A comparison of the preliminary U.S. forecast with the forecast adopted in November is shown in Table 2.

The Washington State forecast reflects the slightly stronger growth in the new U.S. forecast. The Washington aerospace employment forecast is not as weak in the first quarter of 2004 but otherwise is essentially unchanged. The forecast expects a decline of 2,100 during 2004 before a modest recovery begins in 2005 which adds 11,200 by the end of 2007. Though software wages probably fell sharply in the fourth quarter due to a decline in stock option activity, the software wage assumption for 2004 and 2005 is virtually identical to the assumption made in November. The forecast still assumes there will be no major fluctuations in Microsoft stock option activity in the future. The software employment forecast assumes an increase of about 4,000 employees per year through 2007.

This forecast also incorporates newly available Covered Employment and Payrolls (ES-202) data for the third quarter of 2003. The benchmark revision to September

employment added 10,300 to the level of employment in September however the growth during the rest of the year was slightly less than expected. The net effect was an increase in December of 7,300. The ES-202 data also indicate that third quarter wages were \$2.226 billion higher than expected in November mostly due to a \$1.513 billion discrepancy in software wages. Non-software wages were also higher than expected by \$0.713 billion. Nonwage personal income was \$0.305 billion higher than expected in November resulting in an upward revision to total personal income of \$2.531 billion. The forecast also reflects Seattle consumer price data through December, which shows local inflation running well below the national average. Seattle's December-over-December inflation was only 0.5 percent while the core index actually fell 0.3 percent over the year. Washington housing activity moderated in the fourth quarter from the frenzied pace of the third quarter. The number of units authorized by building permit decreased by 4,300 to a still strong 41,000.

A comparison of the preliminary Washington forecast with the forecast adopted in November is shown in Table 3.

Review of the forecast by the Governor's Council of Economic Advisors is scheduled for Friday February 6, 2004 at 10:00 a.m., in the **Insurance Building 4<sup>th</sup> floor conference room**.

If you have any questions, please contact Bret Bertolin, Senior Economic Forecaster, at (360) 570-6106.

**PLEASE NOTE:**

Enclosed is a worksheet summarizing the preliminary forecast. **Council members are strongly encouraged to complete and return this worksheet either in person at the Governor's Council meeting or, if unable to attend, by FAX to (360) 753-7022.** This worksheet is relied on by the Forecast Council members and staff to gauge the reasonableness of the preliminary economic forecast and also serves as the basis of an alternative economic and revenue forecast.

Fluctuations in software wages due to stock option income have, in the past, caused significant distortions in overall wage and personal income trends. The forecast assumes a rebound in option income in the first quarter of 2004 from an extremely low level in the fourth quarter of 2003. Except for the first quarter of 2004, these distortions are expected to be small as shown in the table below.

Preliminary January Economic Forecast  
February 3, 2004  
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	2004:1	2004	2005	2006	2007:1,2
<u>Washington Real Personal Income, %Ch.</u>					
Baseline	6.1	3.4	3.9	4.2	4.2
Excluding Software	2.8	3.4	3.8	4.0	4.1
Software's Impact	3.2	0.0	0.1	0.1	0.1
<u>Washington Average Annual Wage, %Ch.</u>					
Baseline	9.9	2.8	3.6	4.1	4.7
Excluding Software	3.8	3.0	3.5	3.9	4.6
Software's Impact	5.9	-0.1	0.1	0.2	0.1

CMS: dym/bb  
Enclosures

Table 1  
**U.S. Economic Forecast Comparison**  
January 2004

	2003:4	2004:1	2004:2	2004:3	2004	2005	2006	2007
<b>Real GDP, Percent Change</b>								
Global Insight	4.7	4.0	3.9	5.0	4.7	4.0	3.4	3.3
Blue Chip	4.3	4.4	4.2	4.0	4.6	3.7		
Economy.com	4.4	4.2	3.4	3.2	4.3			
S&P	4.7	4.0	4.2		4.5	3.4	3.3	
Merril Lynch	4.0	3.0	5.0	3.5	4.3			
<b>Federal Funds Rate</b>								
Global Insight	1.00	1.00	1.00	1.50	1.30	2.37	3.00	3.19
Blue Chip*	1.0	1.1	1.3	1.5	1.4	2.7		
Economy.com	1.00	1.00	1.03	1.41	1.35			
S&P	1.0	1.0	1.0	1.0	1.0	1.9	3.0	
Merril Lynch	1.00	1.00	1.00	1.00	1.00			
<b>Consumer Price Index, Percent Change</b>								
Global Insight	0.9	2.2	0.5	1.2	1.4	1.3	1.5	1.9
Blue Chip	1.3	1.7	1.8	1.9	1.7	2.1		
Economy.com	1.1	1.1	1.1	1.1	1.2			
S&P	1.6	0.9	0.9		1.4	1.5	1.7	
Merril Lynch	1.7	0.2	1.1	1.4	1.1			
<b>Payroll Employment, Millions</b>								
Global Insight	130.1	130.5	131.5	132.5	132.0	135.4	137.7	139.7
Economy.com	130.1	130.5	131.0	131.7	131.4			
S&P	130.1	130.6	131.2		131.5	133.6	136.0	
<b>Unemployment Rate, Percent</b>								
Global Insight	5.87	5.81	5.72	5.61	5.65	5.30	5.29	5.27
Blue Chip	5.9	5.9	5.8	5.7	5.7	5.4		
Economy.com	6.1	6.2	6.2	6.1	6.1			
S&P	5.7	5.7	5.6		5.6	5.5	5.5	
Merril Lynch	5.9	5.9	5.9	5.8	5.9			
<b>Real Disposable Personal Income, Percent Change</b>								
Global Insight	0.3	5.9	3.2	4.5	4.1	3.8	3.4	2.9
Blue Chip	1.9	5.9	3.8	2.7	4.2	3.4		
Merril Lynch	2.7	3.3	5.0	4.0	4.1			

\* Estimate based on T-bill rate.

Table 2

**U.S. Forecast Comparison**

	2003:2	2003:3	2003:4	2004:1	2004:2	2004:3	2001	2002	2003	2004	2005
<b>Real GDP (Billions of Chained 2000 Dollars)</b>											
January	10288.3	10493.1	10614.5	10719.7	10823.7	10956.0	9866.7	10083.1	10401.6	10895.1	11325.9
Percent Change	3.1	8.2	4.7	4.0	3.9	5.0	0.5	2.2	3.2	4.7	4.0
October	9629.4	9761.1	9867.9	9958.4	10051.3	10166.6	9214.5	9439.9	9702.6	10110.7	10488.6
Percent Change	3.3	5.6	4.4	3.7	3.8	4.7	0.3	2.4	2.8	4.2	3.7
<b>Implicit Price Deflator (2000=1.000)</b>											
January	1.051	1.055	1.056	1.060	1.062	1.065	1.020	1.034	1.053	1.064	1.079
Percent Change	0.5	1.7	0.2	1.8	0.7	1.2	2.0	1.4	1.8	1.1	1.4
October	1.128	1.135	1.138	1.140	1.143	1.149	1.096	1.111	1.132	1.147	1.168
Percent Change	0.8	2.3	1.0	0.9	1.1	1.8	2.0	1.4	1.9	1.3	1.8
<b>Real Personal Income (Billions of Chained 2000 Dollars)</b>											
January	8705.0	8758.8	8830.5	8900.3	8991.7	9092.0	8539.0	8614.8	8729.5	9044.6	9420.7
Percent Change	3.8	2.5	3.3	3.2	4.2	4.5	1.3	0.9	1.3	3.6	4.2
October	8113.9	8152.3	8227.0	8328.6	8410.0	8486.9	7927.3	8033.3	8139.0	8446.5	8749.6
Percent Change	2.6	1.9	3.7	5.0	4.0	3.7	1.3	1.3	1.3	3.8	3.6
<b>Wage and Salary Employment</b>											
January	129.98	129.90	130.11	130.54	131.47	132.47	131.83	130.38	130.06	131.96	135.41
Percent Change	-0.7	-0.3	0.6	1.3	2.9	3.1	0.0	-1.1	-0.2	1.5	2.6
October	129.98	129.84	129.99	130.32	130.98	131.89	131.83	130.38	130.01	131.50	134.65
Percent Change	-0.7	-0.4	0.5	1.0	2.1	2.8	0.0	-1.1	-0.3	1.1	2.4
<b>Unemployment Rate</b>											
January	6.13	6.13	5.87	5.81	5.72	5.61	4.76	5.78	5.99	5.65	5.30
October	6.17	6.13	6.20	6.16	6.15	6.05	4.77	5.78	6.07	6.08	5.88
<b>Mortgage Rate</b>											
January	5.51	6.01	5.93	6.15	6.31	6.61	6.97	6.54	5.82	6.46	6.99
October	5.51	6.03	6.09	6.13	6.20	6.33	6.97	6.54	5.87	6.27	6.77
<b>3 Month T-Bill Rate</b>											
January	1.04	0.93	0.92	0.97	0.98	1.42	3.43	1.61	1.01	1.24	2.17
October	1.04	0.96	0.94	0.95	0.95	0.99	3.43	1.61	1.03	1.02	1.71

Table 3

**Washington Forecast Comparison**

	2003:2	2003:3	2003:4	2004:1	2004:2	2004:3	2001	2002	2003	2004	2005
<b>Real Personal Income (Billions of Chained 2000 Dollars)</b>											
January	195.783	198.518	196.422	199.343	201.265	203.409	187.818	191.649	195.834	202.395	210.335
Percent Change	6.7	5.7	-4.2	6.1	3.9	4.3	0.5	2.0	2.2	3.4	3.9
October	182.432	182.360	183.154	185.137	186.731	188.166	174.919	178.472	181.941	187.404	193.571
Percent Change	5.9	-0.2	1.8	4.4	3.5	3.1	0.5	2.0	1.9	3.0	3.3
<b>Personal Income</b>											
January	205.690	209.470	207.378	211.392	213.797	216.695	191.644	198.221	206.158	215.428	227.056
Percent Change	7.3	7.6	-3.9	8.0	4.6	5.5	2.6	3.4	4.0	4.5	5.4
October	205.858	206.939	208.359	211.109	213.489	216.113	191.644	198.221	205.915	214.884	226.012
Percent Change	6.8	2.1	2.8	5.4	4.6	5.0	2.6	3.4	3.9	4.4	5.2
<b>Wage and Salary Employment</b>											
January	2652.1	2659.9	2665.6	2670.4	2687.6	2706.6	2697.4	2653.2	2658.3	2697.1	2764.4
Percent Change	-0.5	1.2	0.9	0.7	2.6	2.9	-0.5	-1.6	0.2	1.5	2.5
October	2657.7	2652.5	2655.6	2662.1	2674.3	2689.8	2697.4	2654.1	2656.8	2682.9	2744.2
Percent Change	-0.6	-0.8	0.5	1.0	1.8	2.4	-0.5	-1.6	0.1	1.0	2.3
<b>Manufacturing Employment</b>											
January	268.6	265.0	261.9	260.9	260.8	260.0	316.2	285.5	267.3	260.1	261.3
Percent Change	-7.5	-5.3	-4.6	-1.5	-0.1	-1.3	-4.7	-9.7	-6.4	-2.7	0.5
October	269.2	266.6	264.7	262.7	262.5	262.0	316.2	285.7	268.7	262.3	264.3
Percent Change	-7.3	-3.7	-2.9	-2.9	-0.4	-0.8	-4.7	-9.6	-5.9	-2.4	0.8
<b>Construction Employment</b>											
January	155.0	156.3	158.4	159.4	160.0	160.3	158.8	154.4	156.3	160.2	164.4
Percent Change	-1.4	3.4	5.6	2.5	1.4	0.7	-1.1	-2.8	1.2	2.5	2.6
October	156.0	157.7	158.7	159.3	159.8	160.1	158.8	154.8	157.3	160.0	163.5
Percent Change	-2.3	4.3	2.7	1.4	1.4	0.6	-1.1	-2.5	1.6	1.7	2.2
<b>Housing Permits</b>											
January	42.840	45.258	40.966	40.952	40.455	41.004	38.345	40.200	43.159	40.945	40.570
Percent Change	-6.6	24.6	-32.9	-0.1	-4.8	5.5	-1.7	4.8	7.4	-5.1	-0.9
October	42.840	45.258	42.231	41.044	40.603	40.547	38.345	40.200	43.476	40.733	39.493
Percent Change	-6.6	24.6	-24.2	-10.8	-4.2	-0.5	-1.7	4.8	8.1	-6.3	-3.0

Advisor's Name: \_\_\_\_\_

**Forecast Worksheet**  
**February 3, 2003**

	2004:Q1	2004	2005	2006	Average 2007:1,2
<b><u>U.S.</u></b>					
<b>Real GDP, %Ch</b>					
Baseline	4.0	4.7	4.0	3.4	3.0
Your Opinion	_____	_____	_____	_____	_____
<b>Implicit Price Deflator, % Ch</b>					
Baseline	1.8	1.1	1.4	1.8	2.3
Your Opinion	_____	_____	_____	_____	_____
<b>Mortgage Rate, Percent</b>					
Baseline	6.2	6.5	7.0	7.0	6.9
Your Opinion	_____	_____	_____	_____	_____
<b><u>Washington State</u></b>					
<b>Real Personal Income, % Ch</b>					
Baseline	6.1	3.4	3.9	4.2	4.2
Your Opinion	_____	_____	_____	_____	_____
<b>Wage and Salary Employment, % Ch</b>					
Baseline	0.7	1.5	2.5	2.1	2.0
Your Opinion	_____	_____	_____	_____	_____
<b>Manufacturing Employment, % Ch</b>					
Baseline	-1.5	-2.7	0.5	2.6	2.4
Your Opinion	_____	_____	_____	_____	_____
<b>Construction Employment, % Ch</b>					
Baseline	2.5	2.5	2.6	2.3	2.7
Your Opinion	_____	_____	_____	_____	_____
<b>Housing Permits (Thousands)</b>					
Baseline	41.0	40.9	40.6	39.2	40.3
Your Opinion	_____	_____	_____	_____	_____
<b>Washington Average Annual Wage, % Ch</b>					
Baseline	9.9	2.8	3.6	4.1	4.7
Your Opinion	_____	_____	_____	_____	_____